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SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1946

No. 603

MATILDA J. FELDMAN,

Petitioner,

vs.

PENNROAD CORPORATION, A CORPORATION OF THE STATE OF DELAWARE,

Respondent

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT AND BRIEF IN SUPPORT THEREOF.

To the Honorable, The Chief Justice and the Associate Justices of the Supreme Court of the United States:

The petitioner respectfully prays for a writ of certiorari to the United States Circuit Court of Appeals for the Third Circuit to review its decision and judgment rendered on May 21, 1946 (R. 47) in Matilda J. Feldman *vs.* Pennroad Corporation, a corporation of the State of Delaware, 155 F. (2d) 773, which affirmed the order of the United States District Court for the District of Delaware granting the motion of the defendant dismissing the amended complaint

which said judgment of the District Court was filed May 25, 1945. The District Court denied reargument on June 13, 1945. The District Court's opinion appears at 60 F. Supp. 716.

Summary Statement of the Matter Involved

Matilda J. Feldman, the petitioner, is a stockholder of Pennroad Corporation (hereinafter called "Pennroad").

By petition sworn to March 8, 1945, Pennroad Corporation applied to the Chancery Court of the State of Delaware for a hearing on the approval of a proposed settlment with the Pennsylvania Railroad Company of certain pending litigation. The Chancery Court set April 23, 1945, as the return day for the hearing on the proposed settlement.

On April 16, 1945, Matilda J. Feldman commenced an action in the United States District Court for the District of Delaware in which she sought *inter alia* the appointment of a receiver for Pennroad with power to prosecute suits on behalf of Pennroad and for an injunction against the making by Pennroad of any settlement or other disposition of its claims against the Pennsylvania Railroad Company, its directors and officers.

The amended complaint, against which the motion to dismiss was directed, alleged as follows:

That there is diversity of citizenship between the parties; that the matter in controversy is in excess of the jurisdictional value and that the plaintiff is acting not only for herself but in behalf of the holders of approximately 10,000 shares of stock of the defendant (paragraphs 1 to 3 inclusive).

That The Pennsylvania Railroad Company (hereinafter referred to as Pennsylvania) in order to extend its influence and build up its railroad empire by acquisition of controlling blocks of securities in various railroads which

it was unwilling to acquire for its own account because the securities thereof were highly speculative, the prices demanded therefore were excessive and such acquisitions by it were illegal and contravened the laws of the United States and the rules and regulations of the Interstate Commerce Commission, organized the defendant to make such purchases and caused the defendant to sell its securities to the general public; that the plaintiff purchased such securities in 1929 and has continued to hold such securities ever since and was therefore the owner of such securities during the times of the commission of all the wrongs complained of in the complaint (paragraphs 4 to 6 inclusive).

That in furtherance of the aforesaid unlawful plan and conspiracy, Pennsylvania in 1929 caused a ten year voting trust covering all the securities of the defendant to be entered into and that the voting trustees were officers of Pennsylvania and that therefore Pennsylvania had complete domination of the defendant without any investment of any kind, nature or description therein, and the public, with an investment of approximately $140,000,000 had no control or influence of any kind and in fact under the provisions of the certificate of incorporation and the by-laws, was precluded from even securing information concerning the operation of the defendant; that in the acquisition of securities the directors of the defendant were the dummies of Pennsylvania, exercised no independent judgment but merely carried out the mandates of Pennsylvania (paragraphs 7 to 10 inclusive).

That the directors of the defendant have at all times been and now are under the domination and control of Pennsylvania and that the defendant at no time has ever had counsel wholly independent and acting solely for the best interests of the defendant, but that to the contrary, counsel likewise have been under the domination and control of Pennsylvania and that all of the assets of the defendant

have been fraudulently and improperly used for the benefit of Pennsylvania and to the detriment of the defendant and its shareholders (Paragraphs 11 to 14 inclusive).

That in carrying out the aforesaid illegal and unlawful plan of conspiracy, domination and misuse of the defendant's funds, great losses have been caused to the defendant (1) by the acquisition of securities at excessive and fraudulent prices purchased without any regard to their intrinsic merit or value, but solely for the purpose of furthering the benefits to Pennsylvania; (2) by the operation of the companies whose securities were purchased as above for the benefit of Pennsylvania, and in violation of the rights of the defendant and its security holders, and (3) by incurring large underwriting expenses in the securing of funds which were not necessary for the defendant's business but which were necessary only to enable the defendant to secure securities as above described, desired for Pennsylvania and used for its benefits (paragraphs 15 to 17 inclusive).

That in order to secure restitution in part for certain of the wrongs above described three stockholders' suits were begun, two of which have been dismissed on the ground that the statute of limitations had run out but not on the merits. That the third is still pending and that the directors wholly controlled and dominated by Pennsylvania have at all times resisted the prosecution of such suits to the detriment of the defendant to prevent its securing redress for the wrongs perpetrated (paragraphs 18 and 19).

That none of the aforesaid suits has been brought to compel an accounting for profits illegally made or wrongful acts done subsequent to the acquisition of the shares hereinabove described, the last of which acquisitions took place in June, 1931 (paragraph 20).

That in furtherance of the aforesaid conspiracy and scheme, Pennsylvania is now endeavoring to foist upon the

hapless, defenseless defendant corporation a wholly inadequate settlement of $15,000,000 in complete satisfaction and discharge not only of the wrongs in respect of the acquisitions for which the aforementioned three stockholders' suits were brought, but in addition for wrongs perpetrated subsequent to such acquisitions and for which no relief has been sought in the pending stockholders' suits and endeavoring to dismiss pending suits; that the directors of the defendant corporation who are completely dominated and controlled by Pennsylvania have joined with Pennsylvania to carry out such illegal plan and purpose by entering into an agreement of settlement and by endeavoring to secure judicial approval therefor by petition filed with the Chancery Court of the State of Delaware (paragraphs 21 to 23 inclusive).

That the attempt of the defendant to condone the wrongs of Pennsylvania and its own directors by the consummation of the proposed settlement may not be achieved without the consent of the plaintiffs in the three pending stockholders' actions and should not be permitted without a full and complete disclosure of all material and pertinent facts to approximately 100,000 holders of 6,000,000 shares of the defendant's stock presently issued and outstanding (paragraphs 24 and 25).

That as the directors of the defendant are controlled and dominated by Pennsylvania it is impossible for them to adequately protect the interests of the stockholders before the Chancery Court of Delaware or before any other court and it is therefore essential that an impartial receiver or receivers be appointed not only to consider the merits of the proposed settlement but to make a full investigation in respect thereto and to make fair and proper presentation in respect of any application to confirm or approve the same, or in the event such investigations should justify

the same, to institute such other actions or proceedings as may be warranted or necessary for the protection of the rights of the defendant and its security holders (paragraphs 26 to 29 inclusive).

That the merit of the defendant's claims against Pennsylvania has been established in the actions now pending in the United States District Court for the Eastern District of Pennsylvania and by the dissenting opinion of Judge Biggs, Jr., Senior Circuit Court Judge (paragraph 30).

That the plaintiff has no adequate remedy at law and unless the acts of the defendant and its directors are stayed and a receiver appointed, the plaintiff and other stockholders of the defendant and the defendant itself, will suffer irreparable harm and injury. That demand upon the directors to institute this action would be futile and the action is not a collusive one to confer jurisdiction on the District Court (paragraphs 31 to 35 inclusive).

The Pennroad Corporation moved to dismiss the action on the ground that the complaint failed to state a claim upon which relief could be granted. The District Court for the District of Delaware dismissed the complaint on May 25, 1945, refusing both an injunction and the appointment of a receiver.

In dismissing the complaint the District Court relied among other things on the following (R. p. 27a) which were *dehors* the complaint:

1. That there was nothing to prevent plaintiff from fully presenting the facts alleged in the District Court action to the State Court (Chancery Court of the State of Delaware).

2. That counsel for the plaintiff, Feldman, and counsel for Perrine during the argument of the motion allegedly said that the State Court had permitted them to present fully their objections to the settlement in the hearings there.

3. That the Court must assume that the State Court would do justice to all parties and if there is merit in the allegation presented in the District Court complaint that the State Court would grant adequate relief.

4. That the allegation of the complaint of the imminent danger of a collusive settlement would be persuasive if the settlement were contemplate dwithout court approval, but the Federal District Court must assume that Pennroad and its stockholders would be adequately protected by the hearings then to be held in the State Court *to obtain judicial approval of the settlement* (R. pp. 28a-29a).

Counsel for petitioner made a motion for reargument on June 4, 1945 on the ground that counsel had never stated upon the argument that the State Court had permitted them to present fully their objections to the settlement in the hearing there. Motion for reargument was denied on June 13, 1945.

On August 13, 1945, the Court of Chancery of Delaware approved the settlement and authorized the same carried out. The Vice-Chancellor in approving the settlement held that since he concluded that in entering the settlement the Pennroad Directors were free from disqualifying interests and acted in good faith, there was *no need for him to inquire into the merits of the settlement.* (43A 2d 721, 728).

On August 24, 1945, the plaintiff (the petitioner herein) filed a notice of appeal to the United States Circuit Court of Appeals for the Third Circuit from the order of the United States District Court for the District of Delaware dismissing the complaint of the petitioner herein.

In the Crcuit Court of Appeals the petitioner herein argued that the complaint stated grounds for a cause of action in equity and should not have been dismissed because of the assumptions made by the District Court that the Delaware Chancery Court would permit a full hearing on

the petitioner's objections and that Pennroad and its stockholders would be adequately protected. It was further argued that since the decision of the District Court had been rendered, the Delaware Chancery Court had entered an order on the opinion of the Vice Chancellor which established the fact that the assumption by the District Court was wholly erroneous, for in said opinion it was stated specifically that there was no need to inquire into the merits of the settlement.

Petitioner herein also argued in the Circuit Court of Appeals that Rule 23(c) of the Federal Rules of Civil Procedure had been violated inasmuch as the Delaware Chancery Court had approved an agreement of settlement providing for the disposition of actions pending in the Federal Court.

Thereafter, the Supreme Court of the State of Delaware handed down its decision approving the decree of the Vice Chancellor. On May 21, 1946, the United States Circuit Court of Appeals for the Third Circuit affirmed the judgment of the District Court for the District of Delaware.

Jurisdiction

1. The jurisdiction of the court is invoked under Section 240 of the Judicial Code as amended; 28 U. S. C. A. Section 347. The judgment of the Circuit Court of Appeals for the Third Circuit was entered on May 21, 1946 (R. 47). The time in which to present this petition for a writ of certiorari was extended to October 11, 1946.

Statutes

Title 28 U. S. C. A. Sec. 723(b). *Rules in actions at law; Supreme Court authorized to make:*

> "The Supreme Court of the United States shall have the power to prescribe, by general rules, for the district

courts of the United States and for the courts of the District of Columbia, the forms of process, writs, pleadings, and motions, and the practice and procedure in civil actions at law. Said rules shall neither abridge, enlarge, nor modify the substantive rights of any litigant. They shall take effect six months after their promulgation, and thereafter all laws in conflict therewith shall be of no further force or effect. June 19, 1934, c. 651, Sec. 1, 48 Stat. 1064."

Rule 23(c) of the Federal Rules of Civil Procedure, U. S. C. A. Title 28, following Section 723(c), provides as follows:

"(c) Dismissal or Compromise. A class action shall not be dismissed or compromised without the approval of the court. If the right sought to be enforced is one defined in paragraph (1) of subdivision (a) of this rule notice of the proposed dismissal or compromise shall be given to all members of the class in such manner as to court directs. If the right is one defined in paragraphs (a) or (3) of subdivision (a) notice shall be given only if the court requires it."

Questions Presented

1. Whether the decision and judgment of the United States District Court for the District of Delaware affirmed by the Circuit Court of Appeals, which granted the defendant's motion to dismiss the complaint for failure to state a claim upon which relief can be granted, was error.

2. Whether the United States District Court in adjudicating the motion to dismiss the complaint for an injunction to restrain Pennroad from seeking approval of the proposed settlement in the Delaware Chancery on the ground of failure to state a claim upon which relief can be granted, may consider matters *dehors* the complaint, especially where the plaintiff alleged that the Delaware hearing was

brought on by notice not calculated to afford a full and fair hearing in that court.

3. Whether a Federal Court may refuse relief to a suitor in a case where it has jurisdiction of the parties and subject matter on the assumption that suitable relief may be available to the suitor in a state tribunal.

4. Whether an action is pending in the Federal District Court when the District Court has rendered judgment in favor of plaintiff and the Circuit Court of Appeals reversed the judgment bu the mandate of the Circuit Court of Appeals has not gone forward to the District Court and (a) the time for filing petition for rehearing had not expired, and (b) the time had not expired for filing a petition for a writ of certiorari to this Honorable Court.

5. Whether parties to a class action pending in the Federal Court can settle the action in a court other than the Federal Court.

6. Can a United States Circuit Court of Appeals in determining an appeal from a judgment of the District Court dismissing the complaint for failure to state a claim make its decision upon consideration of facts which did not exist at the time of the decision in the District Court and which were not alleged in the complaint.

7. Can the United States District Court for the District of Delaware issue an injunction restraining interference with the jurisdiction of the United States District Court for the District of Pennsylvania in order to preserve the jurisdiction of said Federal Court for the purpose of insuring compliance with the Federal Rules of Civil Procedure and to prevent the circumvention of said Rules.

Specification of Errors

The errors of which petitioner complains and intended to be urged are implicit in the questions presented above and we respectfully request that the same be deemed incorporated herein as though set forth at length.

Reasons for Allowance of the Writ

1. The question presented by this case is an important question because it affects the proper procedure in the compromise and settlement of class actions in the Federal Courts, and if the present decision of the Circuit Court of Appeals is permitted to stand, it would seriously affect the Federal Court's jurisdiction to approve the settlement of class actions there pending.

2. Rule 23 (c) was formulated to place the compromise of class actions under the supervision of the Federal Court to eliminate unsavory practices of private, secret and collusive settlements. The question presented in this case presents the important issue as to whether a settlement of a class action pending in the Federal District Court may be maneuvered into the State Court so that the purpose for which Rule 23 (c) was promulgated is defeated and the protection for which it was designed is emasculated.

3. The writ should be allowed for the reason that the decisions of the Circuit Court of Appeals and the United States District Court erroneously limit and misinterpret the jurisdiction of the Federal Courts. The refusal to enjoin interference with pending litigation in a Federal Court upon the assumption that the suitors would obtain adequate relief in the state tribunal was a decision in conflict with the decision of this Court in *Bank of the United States* v. *Deveaux*, 5 Cranch 61, 87; 3 L. Ed. 38, and other decisions of this Court.

4. The decision that the *Overfield-Weigle* case in the United States District Court for the Eastern District of Pennsylvania and the Circuit Court of Appeals for the Third Circuit was not pending, was a decision in conflict with the decision in *Dickheiser* v. *The Pennsylvania Railroad Company*, 5 F. R. D. 5 and other decisions of the Federal Courts and local and general law.

5. The decision of the District Court and Circuit Court of Appeals on testing the sufficiency of the complaint upon the motion to dismiss by reference to assumptions of fact outside the record was a decision in conflict with the decisions of this court, the Federal Courts, and well settled authority.

Respectfully submitted,

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BRIEF IN SUPPORT OF PETITION

ARGUMENT

Point I

The District Court for the District of Delaware upon the determination of the motion to dismiss committed error in going dehors the allegations of the complaint, which are taken as true upon such a motion.

The motion to dismiss the complaint under Rule 12 of the Rules of Civil Procedure is limited to the allegations of the complaint and facts not appearing therefrom must be disregarded upon the motion. *Mullens, et al.* v. *DeSoto Securities Co., Inc., et al.*, 136 F. (2d) 55; *Rozelle* v. *Quinn*, 47 F. Supp. 740; *Grodsky* v. *Sipe*, 30 F. Supp. 656; *Massachusetts Mut. Life Ins. Co.* v. *Grossman, et al.*, 4 F. Supp. 990; Equity Rule 29, 28 U. S. C. A. Foll. Sec. 723.

In *Rozelle* v. *Quinn, supra*, at page 741 the Court said:

> "The motion to dismiss is limited to the allegations of the petition * * * facts not appearing therefrom must be disregarded upon this motion. (cases cited) * * * In accordance with the rule, the scope of the examination here will be restricted to the four corners of the complaint."

The District Court in its opinion assumed that the Chancery Court of Delaware would inquire into the merits of the settlement. The District Court in its opinion (R. p. 27a) said:

> "This Court must assume that the State Court will do justice to all parties, and, if there is merit in the allegations herein presented, that the State Court will grant whatever relief may be just and proper."

This assumption is wholly unsupported by anything found within the four corners of the complaint, the allega-

tions of which on the motion to dismiss must be taken as true and must be construed in the light most favorable to the plaintiff: *Cool* v. *International Shoe Co.*, 142 F. (2d) 318; *Ledbetter* v. *Farmers Bank & Trust Co.*, 142 F. (2d) 147; *Noonan* v. *Fruco Const. Co.*, 140 F. (2d) 633.

In *Cool* v. *International Shoe Co.*, 142 F. (2d) 318, the Court at page 320 said:

> "Plaintiff was entitled to a liberal construction of his complaint. We have held that on a motion to dismiss for insufficiency of statement, the complaint should be construed in the light most favorable to the plaintiff and with all doubts resolved in his favor. Leimer *v.* State Mutual Assurance Co., 8 Cir. 108 F. 2d 302. In Musteen *v.* Johnson, 8 Cir. 133 F. 2d 106, 108, it was held error to dismiss a complaint on the ground of insufficiency of statement unless 'it appears to a certainty that the plaintiff would be entitled to no relief under any state of facts which could be proved in support of the claim asserted by him.' "

The vice of dismissing a complaint on the basis of assumptions *dehors* the complaint is well illustrated by the instant case. Contrary to Judge Bard's expectations and assumptions as to the role and duty of the Delaware Court, that court flatly refused to inquire into the merits of the settlement. Vice Chancellor Pearson in approving the settlement held:

> "From the evidence, I conclude and find that in entering the settlement the directors were free from disqualifying interests, and that they acted in good faith. With that finding, there is no need to inquire into the merits of the settlement."

Thus litigation of vast importance is concluded without any inquiry into the merits of the settlement.

All of which points up the force and efficacy of the elementary principle that a complaint valid on its face may not be dismissed on motion.

Point II

The decisions below erroneously limited and restricted the jurisdiction of the Federal Court and denied the Pennroad stockholders the protection of court approval of the settlement to which they were entitled in the Overfield-Weigle Case under Federal Rule 23(c).

The petitioner argued in the District Court and in the Circuit Court of Appeals that Rule 23(c) of the Federal Rules of Civil Procedure, made it necessary for the Pennroad Corporation to apply to the District Court for the Eastern District of Pennsylvania for approval of the compromise agreement with the Pennsylvania Railroad Company for the reason that the agreement provided as a condition precedent to the payment of the money, that the Overfield-Weigle suit be so disposed of that the mandate of the Circuit Court of Appeals dismissing the suit should go forward to the District Court and the complaints dismissed in accordance therewith.

The petitioner also argued that the Overfield-Weigle suits were still pending in the District Court, a fact which was found by Bard, J., in *Dickheiser* v. *The Pennsylvania Railroad Company,* 5 F. R. D. 5, 10, where Judge Bard said as follows:

> "Complainants' allegation of fraud and neglect of duty on the part of the directors in approving the settlement is based on an erroneous interpretation of the legal effect of the Circuit Court decision in the Overfield-Weigle case. Complainants allege that the Overfield-Weigle case has reached final judgment. But how can this be true when the time for filing a petition for rehearing has been extended and is unexpired? There is no certainty that a petition for rehearing will be denied or that a petition for a writ of certiorari will be unfruitful."

That the action is still pending is amply supported by numerous cases in various Federal jurisdictions. Rules 35 and 38 of the Circuit Court of Appeals, Third Circuit; *Omaha Electric Light & Power Co.* v. *City of Omaha,* 216 Fed. 848; *Burget* v. *Robinson,* 123 Fed. 262; *Becker Steel Co.* v. *Hicks,* 66 F. 2d 497; *Winkelman* v. *General Motors Co.,* 48 F. Supp. 490; *In re Carlisle Packing Co.,* 12 Supp. 11; *Ex Parte Craig,* 274 Fed. 177.

As was said in *Omaha Electric Light & Power Co.* v. *City of Omaha, supra,* at page 855:

> "It is a universal rule that the perfecting of an appeal transfers the cause to the appellate court, and that it remains there until it is remitted to the trial court by the sending down of the mandate."

Apparently the Circuit Court of Appeals misconceived the argument with respect to rule 23(c). In its opinion the Circuit Court of Appeals held as follows with respect to the argument of the petitioner as the Court conceived it:

> "The plaintiff urges that in the federal court she is entitled to have the court itself consider the adequacy of the consideration. She calls attention to Civil Procedure Rule 23(c) which provides that "A class action shall not be dismissed or compromised without the approval of the court * * *". But this rule refers to action by the court in which the class suit is pending. It may well be that if the Overfield-Weigle suits had not been finally decided by this court but were still pending undetermined in the District Court for the Eastern District of Pennsylvania and an application had been made to that court for leave to dismiss them pursuant to a compromise settlement that court would have had authority to consider independently the wisdom and sufficiency of the settlement. The court below, however, was not in that position. No class suit was pending before it. * * *"

The petitioner herein did not urge in the courts below that the Delaware court could consider the settlement provided it followed the procedure laid down by the Federal cases interpreting rule 23(c). The petitioner urged that the existence of rule 23(c) made it impossible for the Delaware courts to consider or approve the settlement at all in the light of the pendency of the Overfield-Weigle action sought to be disposed of in the Delaware proceeding.

Point III

The decisions below erroneously denied the plaintiff her option to resort to the Federal Court for the relief to which she was entitled.

The complaint having alleged diversity of citizenship and the other jurisdictional requirements it was incumbent upon the District Court to retain jurisdiction and not to refer plaintiff to the State Court upon an assumption that adequate relief would be available there. The main reason for the existence of federal jurisdiction is to provide a non-resident a forum of assured impartiality. The plaintiff exercised her constitutional option in the selection of the forum. It was the obligation of the Federal Court to give effect to the exercise of such constitutional rights. *Doench Duhme & Co.* v. *Federal Deposit & Ins. Corporation,* 315 U. S. 447, 62 S. Ct. 676; *Baltimore & Ohio Railroad Co. et al.,* v. *Wabash Railroad Co.,* 119 Fed. 678, C. C. A. 7, at 680; *Bank of United States* v. *Deveaux,* 5 Cranch 61, 87, 3 L. Ed. 38.

In *Bank of United States* v. *Deveaux, supra,* Chief Justice Marshall said:

> "However true the fact may be, that the tribunals of the states will administer justice as impartially as those of the nation, to parties of every description,

> it is not less true that the Constitution itself either entertains apprehensions on this subject, or views with such indulgence the possible fears and apprehensions of suitors, that it has established national tribunals for the decision of controversies between aliens and a citizen, or between citizens of different states."

The decision of the Circuit Court also results in a most anomalous situation. The District Court abdicated jurisdiction and dismissed the complaint on the assumption now established as erroneous that there would be an adequate hearing and determination in the Delaware Chancery Court. From that dismissal petitioner herein appealed to the Circuit Court of Appeals, Third Circuit, and when the appeal came on to be argued, petitioner herein pointed out to said Court the decision of the Vice Chancellor in Delaware which established how wrong was the assumption of the District Court.

Thereafter, but prior to the decision of the Circuit Court in the instant case, the Supreme Court of Delaware, handed down its decision affirming the decree of the Chancery Court which was made as above set forth without any inquiry into the merits of the settlement. Therefore at the time of the Circuit Court decision, the erroneous assumption by the District Court was not only established by the Chancery Court of Delaware but also confirmed by the Supreme Court of that state. The Circuit Court notwithstanding, held that petitioner herein was estopped by the judgment in the Delaware proceeding.

Conclusion

The amended complaint set forth a valid cause of action over which the Federal Court had jurisdiction. The motion to dismiss should have been denied and the decisions below

constituted reversible error, for which a writ of certiorari should issue.

Respectfully submitted,

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IN THE

Supreme Court of the United States.

No. 603. October Term, 1946.

MATILDA J. FELDMAN,

Petitioner,

v.

THE PENNROAD CORPORATION.

BRIEF ON BEHALF OF RESPONDENT AGAINST PETITION FOR CERTIORARI.

I. PRELIMINARY STATEMENT.

The present petition represents *one of four separate and distinct attempts* to have the Supreme Court of the United States review the approval by the Supreme Court of Delaware of an agreement, dated March 2, 1945, between The Pennroad Corporation, hereinafter called "Pennroad", and The Pennsylvania Railroad Company, hereinafter called "Pennsylvania", settling for $15,000,000.00 the litigation involving these two corporations and their directors, which litigation has been going on since 1932.

1. Situation Prior to Beginning of Present Action.

This litigation consisted of (1) a suit in the Court of Chancery of Delaware, the Perrine suit, begun in 1932, and (2) two actions in the District Court of the United States for the Eastern District of Pennsylvania, the Overfield-Weigle cases, begun in 1939 and 1940.

Pursuant to a condition of the settlement agreement, a petition for approval of the settlement was presented by Pennroad to the Court of Chancery of Delaware, in which the Perrine suit was pending.

That court, on March 19, 1945, directed that notice should be given to all shareholders of Pennroad (about 100,000 in number) by mail and by newspaper advertising, that a hearing on the petition would be held before the Vice-Chancellor at Wilmington on April 23, 1945.

2. Present (Feldman) Action.

At this stage of the proceedings, Matilda J. Feldman, *who had not taken any part in any of the litigation from 1932 on,* began the present *entirely new action,* by filing a complaint on April 16, 1945, in the United States District Court for the District of Delaware. The jurisdiction of the court *rested solely on diversity of citizenship.*

The plaintiff stated that she held stock of Pennroad, but did not state how many shares. She stated that she was acting for holders of stock in an amount approximating 10,000 shares (about 6,000,000 shares were outstanding: Record, 14a). She did not state when this stock had been acquired or give the names of any of the persons whom she claimed to represent.

The amended complaint repeated the various allegations concerning the wrongs which Pennsylvania had done to Pennroad, substantially as these wrongs had been set forth in the Perrine suit and in the Overfield-Weigle cases.

It alleged further that the board of directors of Pennroad was about to make a "nefarious" (13a) settlement of the litigation for $15,000,000.00, because the directors of Pennroad were under the control and domination of Pennsylvania (15a), and that the settlement

> "represents a Pennsylvania dictated unconditional surrender of a wholly defenseless, unrepresented, weak respondent." (13a.)

The complaint then stated that Pennroad was endeavoring to obtain court approval for the settlement, and that

a hearing was scheduled in the Chancery Court of Delaware for April 23, 1945. (14a.)

In view of the fact that the board of directors of Pennroad was under the control and domination of Pennsylvania, Feldman alleged that there could not be

> "an impartial, forceful and true representation by the respondent in the proposed hearings on respondent's petition of the true facts." (15a.)

Feldman, therefore, asked that the District Court appoint a receiver for Pennroad and enjoin Pennroad from making a settlement with Pennsylvania.

A hearing on a motion for a temporary restraining order and the appointment of a receiver pendente lite took place on April 20, 1945, and the court agreed at the conclusion of the hearing to sign a restraining order provided Feldman filed a bond.

No bond was filed, and nothing further was done in the Feldman case until April 26, 1945, when the amended complaint was filed.

Pennroad moved to dismiss the complaint, and on May 11, 1945, Judge Bard, specially sitting, filed his opinion dismissing the complaint, (Record, 23a). Feldman appealed to the Circuit Court, which, on May 21, 1946, affirmed the District Court's order, (Record, 42).

3. Proceedings in Perrine Suit.

Meanwhile, a great deal had gone on in the *Perrine suit.*

Beginning on April 23, 1945, and continuing until May 11, 1945, hearings had been conducted in the Court of Chancery of Delaware at Wilmington, before Vice-Chancellor Pearson, on the application of Pennroad for approval of the settlement agreement.

Perrine, through her counsel, Mr. Keenan, and Feldman, (*the same Matilda J. Feldman, who is the plaintiff in this action*), through her counsel, Mr. Brady, did not

merely take part in those proceedings, but *conducted the proceedings.* No other shareholders of Pennroad participated in opposition to the settlement.

During these proceedings, over 1,000 pages of testimony were taken, and ten witnesses were examined, four of them called by Mr. Keenan and Mr. Brady on cross-examination.

There were introduced into evidence at that hearing by Mr. Keenan and Mr. Brady, physical exhibits, including all briefs of all counsel in the Overfield-Weigle cases, covering well over 1,000 pages, and of course all the court opinions handed down by various courts during the years of litigation.

After three months of consideration, the Vice-Chancellor, on August 24, 1935, handed down a decision approving the settlement.

He declared:

> "From the evidence, I conclude and find that in entering into the settlement the directors were free from disqualifying interests, and that they acted in good faith." (43 A. 2d 727, 728).

He further held:

> "Good faith may, nevertheless, be impugned by a showing that the settlement is so unfair and grossly inadequate, from the standpoint of the corporation, as to impel the conclusion that it emanates from acts of bad faith, or a reckless indifference to the rights of others interested, rather than a reasonable exercise of business judgment." (citing cases.)
>
> "The reasonable doubts and possibilities referred to [of getting a judgment in the Perrine case against Pennsylvania] are not susceptible of precise reduction to a numerical ratio by any method of which I am aware. The court is not called upon to make an appraisal in the nature of an advisory opinion. Compare: In

re Midland United Co., D. C. 58 F. Supp. 667, 681. However, the long history of the litigation, the magnitude of the offer in settlement (particularly when compared with the amount of the only damages awarded by any judgment in favor of Pennroad on the basic claims), the testimony of the learned solicitors, Mr. Wolf and Senator Hastings—all viewed in the factual setting of the record before me—furnish full warrant for the conclusion that the acceptance of the offer was within the reasonable exercise of business judgment and did not assail the good faith of the directors." (43 A. 2d 728.)

It may be added that Mr. Keenan and Mr. Brady filed voluminous briefs with the Vice-Chancellor, and after his decision against them, they filed a long petition for a rehearing, and a brief in support of that. This petition was denied.

They then appealed to the Supreme Court of Delaware, and that court unanimously, after consideration of several months, on May 27, 1946, affirmed the decision of the Vice-Cancellor in spite of extensive arguments on behalf of Perrine and Feldman.

The Supreme Court said, among other things:

"It nowhere appears that these directors [the directors of Pennroad] were under the influence of the defendant Pennsylvania Railroad Company." (47 A. 2d 487.)

It also said:

"Wherever it appears that there is fraud or unfair dealing on the part of the Directors in arriving at a settlement, the Court will always take jurisdiction of the case and set aside any settlement arrived at by such means. Karasik v. Pacific Eastern Corporation, 21 Del. Ch. 81, 180 A. 604; Winkelman v. General Motors Corporation, 48 F. Supp. 490." (47 A. 2d 488.)

It also said:

> "We cannot say that the settlement of a $22,104,515.00 judgment for $15,000,000.00 is so grossly inadequate that it shows bad faith on the part of the directors of a corporation who approve it. Considering again the question of whether the Vice-Chancellor should have heard the case on its merits, before determining whether the settlement was a fair and reasonable one, the record discloses that he did hear such testimony from which he might well arrive at the conclusion that the outcome of the litigation was uncertain." (47 A. 2d 489).

Feldman and Perrine have *filed petitions for writs of certiorari* to the Supreme Court of the United States *from the decision* of the Supreme Court of Delaware *in the Perrine case,* but the printed petition and the record have not been filed yet in that action (October Term 1946, No. 595).

4. Other Proceedings in the Supreme Court of the United States.

Just to complete the story, we may add that a *shareholder of Pennsylvania,* named Dickheiser, has filed a petition for certiorari to the Supreme Court of the United States from a judgment of the Circuit Court for the Third Circuit, dismissing his complaint that the settlement was totally unwarranted *from the standpoint of Pennsylvania,* and constituted a complete waste of that corporation's funds.

Finally, Perrine asked an extension of time to file a petition for certiorari to this Court from the judgment of the Circuit Court *in the Overfield-Weigle cases,* but an examination of the record in that court showed that the time for filing such a petition had passed, and the Supreme Court of the United States on September 18th, 1946 therefore refused to grant the extension. (No. , October Term 1946.)

II. QUESTIONS INVOLVED.

Where (1) a stockholders' suit has been commenced in a state court (Delaware) and (2) thereafter another stockholders' action (involving the same matters) is commenced and tried in a federal court, and the Circuit Court of Appeals has dismissed that action, and (3) a petition for approval of the settlement of the entire litigation is presented by the corporation to the Delaware court,

1. Should another federal court (other than the one in which the stockholders' action was pending) sitting in Delaware, appoint a receiver for the corporation and enjoin the proceedings in the Delaware court on the petition to approve the settlement?

2. Is it error for the federal court in such case to assume that the Delaware court will conduct the hearings on the petition with due regard to the rights of all interested parties?

3. After the Supreme Court of Delaware affirms the decision of the Court of Chancery of Delaware approving the settlement, and both these state courts find that the directors of the corporation acted in good faith and within the reasonable exercise of business judgment, was it error for the Circuit Court to affirm the dismissal of a complaint asking the appointment of receivers for the corporation, and an injunction against the proceedings (then already completed) in the state court?

4. Where a stockholder took a principal part in the proceedings in the state court in opposition to the approval of a settlement, appealed to the Supreme Court of the state, and is attempting to appeal from the Supreme Court of the state, to this Court *in that action*, is he not estopped to prosecute *another action* (namely the present action) brought to enjoin the proceedings in the state court, and to have a receiver appointed for the corporation?

5. Where the entire matter before the Supreme Court of the United States has become moot because of the status of the litigation involved, will the Supreme Court grant certiorari?

III. REASONS FOR DENYING CERTIORARI.

This action is a diversity of citizenship case, presenting no constitutional question.

The main reason for denying the petition for certiorari is that the action on which it rests is based solely on allegations all of which have been adjudicated untrue, and asks relief which a federal court could not have granted at the time that the complaint was filed and which the course of events makes it impossible to grant at this time.

The allegations were that the directors of Pennroad in office at the time of the settlement were under the control and domination of Pennsylvania and entered into the settlement at the dictation of Pennsylvania. The relief asked was an injunction against going ahead with proceedings for approval of the settlement by the Court of Chancery of Delaware, and the appointment of receivers for Pennroad.

Judge Bard, sitting in the District Court for District of Delaware, could not under the law have enjoined Pennroad from going ahead in the Court of Chancery of Delaware for any reason—and certainly not on any assumption that that court would not give all parties in interest a fair and impartial hearing and decide the case according to the law of Delaware, *by which laws Judge Bard himself, sitting in a federal court in Delaware, also would be bound.* (Maris, Cir. J. at Record, 45.)

So he could not grant the injunction.

Perhaps he could have appointed a receiver, if he had believed that Pennroad was in imminent danger, but since *the only imminent danger alleged was the making of the settlement,* Judge Bard held that "it must be assumed, as pointed out above, that Pennroad and its stockholders will

be adequately protected from this alleged imminent danger by the Chancery Court of Delaware, where hearings are presently being held to obtain judicial approval of the settlement''. (Record, 28a, 29a.)

By the time that Feldman's appeal to the Circuit Court came up, the proceedings in Delaware had terminated by the approval of the settlement, and the Circuit Court held that after fighting that case, and losing it, Feldman was bound by the determination by the Delaware courts (adverse to Feldman's contention) of the basic facts that the directors of Pennroad acted in good faith, and that there was nothing in the amount of the settlement which stigmatized the directors' acceptance of it as reckless and dishonest (Record 46).

We submit that both the District Court and the Circuit Court decided the case in the only way that they could decide it.

Feldman's remedy, if she had any, was in the state court of Delaware—*and she went in there, alleged all that she had alleged in the present case—and lost.*

Or, if she thought that the federal court which had jurisdiction of the Overfield-Weigle cases was being treated improperly by reason of the proceedings in Delaware, she could have intervened in those cases. She didn't.

She never could hope to get relief from the District Court in Delaware, on the theory that the state courts of Delaware would conduct their proceedings in violation of the law of Delaware or the Constitution of the United States.

IV. DISCUSSION.

1. With Respect to Injunction.

Judge Bard dismissed the prayer to enjoin Pennroad from consummating the settlement, on the ground that he was without power to grant the prayer, in view of Section 265 of the Judicial Code (28 U. S. C. A. Sec. 379) which, with an exception not applicable to our case, prohibits federal courts from granting injunctions "to stay proceedings in any court of a state". (Record 25a.)

The fact that Feldman does not even mention this section or attempt to argue that Judge Bard did not interpret it correctly, is full admission that his conclusion cannot be disputed.

The hearing scheduled before the Court of Chancery obviously was a "proceeding", and the injunction prayed for, if granted, of course would have resulted in staying this proceeding.

This, the federal court may not do: *Toucey v. New York Life Ins. Co.*, 314 U. S. 118, 62 S. Ct. 139.

The suggestion contained in "Reasons for Allowance of the Writ" (Petition, 11), that somehow or other the application to the Delaware court was a manoeuver to circumvent Rule 23 (c), was not made in the complaint in this case.

Rule 23 (c) was not even mentioned in the complaint.

On the contrary, the complaint said that Pennroad required someone other than the Pennsylvania dominated directors "to truly present after investigation *to the Court of Chancery* the facts." (Record 15a.)

There is nothing in the record to show why the proceedings for approval of the settlement were taken in the Perrine suit and not in the Overfield-Weigle cases, and certainly nothing to show any improper motive, but even without anything in the record, it is clear that stockholders were not deprived of their day in court, and it seemed more

natural to proceed in the Perrine suit than in the Overfield-Weigle cases, because (1) the Perrine suit had been brought much earlier than they (1932, instead of 1939), and (2) *it had not been decided,* whereas the Overfield-Weigle cases *had been decided* by the Circuit Court in favor of Pennsylvania.

The federal court whose right to pass in the settlement is supposed by Feldman to have been flouted, dismissed the charge of impropriety in connection with 23 (c) completely, (Record, 45).

2. With Respect to Matter Dehors the Record.

Feldman's chief argument in support of her petition for certiorari seems to be that the District Court dismissed the complaint on the basis of facts not set out in the complaint.

The supposed facts are contained in the following statement in Judge Bard's opinion:

> "This court must assume that the State Court will do justice to all parties, and, if there is merit in the allegations herein presented, that the State Court will grant whatever relief may be just and proper." (Petition, 13.)

If this assumption indeed were a *statement of fact,* we respectfully call attention to the fact that Feldman's complaint nowhere averred that the Court of Chancery *would not do justice* to all parties or if the complaint had merit, *would not grant just and proper relief.*

However, Judge Bard's words are of course *not the statement of any fact.* They are merely the expression of the universally recognized maxim that it will be presumed that in law all things will be done *"rite"*, that is, properly and according to law.

Feldman apparently, without alleging or proving anything to the contrary, contends that Judge Bard should have enjoined the proceedings in the State Court on the ground

that he assumed that the State Court *would not do justice or grant just and proper relief.*

No court could or would make such an assumption.

3. Decisions of Delaware Court and Estoppel of Feldman.

Feldman founded her complaint on the fact allegation that the Pennroad directors were under the domination and control of Pennsylvania, and were being made by Pennsylvania, the tools for a "nefarious" settlement (Record, 13a).

By the time her appeal reached the Circuit Court the Court of Chancery of Delaware had

> "found as a fact after a full hearing that the Pennroad directors acted in good faith in agreeing to the settlement. Moreover, it had found that the sum of $15,000,000 offered in settlement was not so grossly inadequate as to stigmatize the directors' acceptance of it as reckless and dishonest. We note also that the decision of the Court of Chancery was affirmed by the Supreme Court in Delaware and is now final": per Maris, Cir. J. (Record, 46).

In view of this finding how could the Circuit Court in this case stultify itself by sustaining a complaint founded solely on allegations thus *judicially negatived* in the Perrine suit?

Feldman scarcely can claim that the Circuit Court should have shut its eyes to the Delaware courts' decisions, and pretended to be ignorant of them, when Feldman's main criticism of Judge Bard's decision is that an *examination of those very decisions* showed that those courts had refused, as Feldman claims, to inquire into the merits of the settlement. (Petitions 8, 14.)

However that might be if Feldman had not taken an active part in the Delaware litigation, certainly when she was one of the two main actors in it, she is bound by the adjudication.

There then is no escape from the Circuit Court's conclusion:

> "Inasmuch as the plaintiff is now permanently precluded from establishing the factual basis of her alleged cause of action, the dismissal of her complaint must be affirmed." (Record, p. 46.)

4. Whole Matter Is Moot.

Since the decision of the Circuit Court in this case, the judgment of the Circuit Court in the Overfield-Weigle cases has become final.

This Court so ruled, when on September 18th, 1946, it refused to give Perrine, Feldman's co-objector, additional time to file a petition for certiorari in the Overfield-Weigle cases.

With the Overfield-Weigle cases thus finally and completely ended by a judgment in favor of Pennsylvania, and with the Perrine suit ended except for the possibility of the grant of a certiorari by this court *in that suit,* the present case is moot. If this court grants certiorari in the Perrine case, as this same petitioner has asked it to do, the whole issue presented in this case can be presented there. If this court denies certiorari in the Perrine suit, the whole issue presented in this case will have been adjudicated.

There is nothing that can be added to the general situation by prolonging the life of this practically dead action.

5. Conclusion.

Certiorari should be denied.

Respectfully submitted,

Morris Wolf,
Gordon A. Block,
Attorneys for The Pennroad Corporation.

October 31st, 1946.